



STATE BOARD OF EQUALIZATION STAFF LEGISLATIVE BILL ANALYSIS

Date Introduced: **02/23/06**

Bill No: **AB 2533**

Tax: **Sales and Use**

Author: **Leno**

Related Bills:

BILL SUMMARY

This bill would:

- Expand the sales and use tax exemption to include original works of art, as specified, that are leased between nonprofit organizations for a period of 35 years or more, under specified circumstances.
- Expand the exemption to allow a governmental entity to lease a work of art from another entity for public display.
- Clarify that a work of art may include clothing, costumes, dresses, and personal adornment, under specified circumstances.

ANALYSIS

Current Law

Existing law, Revenue and Taxation Code (RTC) section 6365, provides an exemption for sales of original works of art which are purchased by:

- A governmental entity or any nonprofit organization operating a museum under contract for a governmental entity.
- A nonprofit organization, qualified for exemption from state income tax under RTC section 23701d, that purchased the work of art for display in a museum open to the public, as specified, either operated by the purchaser or another nonprofit organization qualified for exemption pursuant to section 23701d.
- Any person donating to the above governmental entity or nonprofit organizations. The transfer must occur and be documented as specified.

In general, the exemption provided to the above described governmental entity or nonprofit organizations, applies only to original works of art which are purchased to become part of the permanent collection of either a museum, a qualified nonprofit organization that is required to loan out its art for display to museums, or a governmental entity which purchases or commissions art for display in public places.

Section 6366.4 exempts purchases of museum pieces only for the San Diego Aero-Space Museum and the California Science Center, and section 6366.3 exempts purchases of display pieces replaced due to destruction by calamity.

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Original works of art are further defined by Board Regulation 1586 as, “tangible personal property which has been created as a unique object intended to provide aesthetic pleasure to the beholder and/or to express the emotions of the artist.” The form of this art includes but is not limited to: visual art, a work of calligraphy, a work of graphic art, crafts, or mixed media.

Under current law, purchases of art, not meeting the criteria of section 6365, and clothing such as dresses, costumes, and personal adornment (e.g. crown, cane, belt, shoes, hat, wig, etc.), are generally subject to the sales or use tax to the same extent as any other sale of tangible personal property not otherwise exempted or excluded by statute.

Proposed Law

This bill amends Section 6365 to provide an exemption from the sales and use tax law for leases of original works of art, as specified, which are leased under specified circumstances, from one nonprofit organization to another for at least a 35 year period.

This bill also provides that the exemption would apply to works of art that are purchased and become part of the permanent collection of a governmental entity that *leases from another entity* art for public display.

Additionally, the statute would be clarified so that purchases of clothing, costumes, dresses, and personal adornment that are works of art as further defined in Regulation 1586(b)(1) would be exempt from tax.

COMMENTS:

- 1. Sponsor and Purpose.** The sponsor of the amendment is the California Historical Society. The purpose of this measure is to allow leases of works of art, including dresses and costumes, between nonprofit organizations to be exempt from tax. The leases will be based on a collection sharing agreement, of not less than 35 years, that allows museums to share parts of their art or history collections that may not be on display, due to the size of the museum, type of collection, or for other reasons, and share them with museums with larger space or similar collections. Structured as a lease, these sharing agreements allow the nonprofit organizations to retain title to their pieces while generating funds to support other exhibits and programs, provide continuing educational material, and enhance the overall enjoyment and appreciation of art.
- 2. What transactions are currently exempt?** The Board has made previous determinations regarding what constitutes a work of art. For example, Sales and Use Tax Annotation 610.0500, suggests that a utilitarian object, such as a dress, could be considered to be a work of art if it is an original work designed to have significant artistic value. It must be hand-crafted by, or under the direction of, an artist or master craftsman, rather than mass produced. If the aesthetic value of the dress is greater than the practical value, then it may be considered a work of art due to its uniqueness and extra effort to “provide aesthetic pleasure to the beholder and/or to express the emotions of the artist.” Additionally, the Board has decided

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that tangible personal property used by an artist in an “assemblage” was considered to be “mixed media,” and exempt as an original work of art. Depending on the exhibit, it is possible for a dress to be exempt if part of an assemblage. According to the sponsor of this bill, most of the pieces involved in the collection sharing agreement are from the 19th and early 20th century.

3. The following terms need clarification. In order to ensure that the amendments accomplish the author’s intent, the following items need to be further defined:

- The proposed amendment expands the exemption to apply to leases of original works of art between *any* nonprofit organizations. Page 1, line 24 and line 25 refer to leases from “one nonprofit organization to another nonprofit organization.” The existing statute, section 6365, limits the exemption to nonprofit organizations as defined in subdivision (a)(2) and (3).
- The proposed subdivision (b)(3), page 2, line 17 uses the term, “*leases from another entity*,” without defining if “entity” is referring to a “person,” as defined in RTC section 6005, or a “governmental entity” as used in section 6365.
- The exemption applies to a work of art that becomes a part of a permanent collection. The proposed law may need to define “permanent collection,” as it applies to leases of original works of art, as a time period of not less than 35 years. Without specifying the definition of “permanent collection,” as it applies to leases, the author may not obtain the exemption for leases as intended.
- Sales of historical clothing that has historical value may still not be exempt from the Sales and Use Tax Law. The exemption provided by section 6365 is intended to cover a work of art and is not a blanket coverage of all items purchased or leased by a museum.

Board staff is willing to work with the author’s office in drafting amendments to the bill that would address these issues.

COST ESTIMATE

Some costs would be incurred in notifying affected retailers, answering inquiries, writing appropriate regulations, and revising returns. A detailed estimate of the workload impacting data entry, verification, and return processing is pending.

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REVENUE ESTIMATE

Background, Methodology, and Assumptions

Existing law provides an exemption for sales of original works of art, as specified, items which have value as museum pieces, as specified, and certain purchases of public art by the state or any local government entity for display to the public, as specified.

This bill would provide an exemption from sales and use tax for leases of original works of art between nonprofit organizations. While staff has been unable to find past examples of this type of an agreement, we are aware of one current example. The agreement allows for the sharing of a collection of assorted paintings and costumes between the California Historical Society and the Autry National Center over several years. As lessee, the Autry National Center would assume general curatorial control of the collection, storage and transit responsibilities, and exhibition space and public access responsibilities. In return, Autry would contribute \$3.5 million to the California Historical Society, over a fifteen year period with payment varying the first three years and fixed from year four through fifteen.

Revenue Summary

For the example above, the revenue loss of exempting lease agreements involving shared collections of original artwork would be computed as follows:

\$3.5 million x 8.5% Tax Rate in San Francisco County = \$297,500

<u>Revenue Loss</u>	
Year 1	\$ 38,250
Year 2	29,750
Year 3	25,500
Year 4-15	17,000 each year
	<u>\$ 297,500</u>

One of the stated goals of the agreement in the above example is to establish a model for future lease agreements. It is reasonable to assume that future revenue impacts would be based on each specific lease agreement. Therefore, it is difficult to estimate with any certainty, the revenue impact of future agreements of this kind.

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